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SUBJECT: MINING FIRMS PROTEST PERMIT DELAYS

¶1. SUMMARY: U.S. and Canadian mining companies have protested the delays in approving their environmental permits for gold mining projects in northern El Salvador. The GOES has indefinitely postponed the issuance of new mining permits while it conducts a study of the environmental impact and economic benefits of the mining sector in El Salvador. Several environmental groups have vocally opposed these projects due to potential groundwater pollution and environmental damage. Funding constraints and political controversy are likely to delay the completion of the study and issuance of new mining permits until after the 2009 elections. END SUMMARY.

¶2. The Ministry of Environment and Natural Resources (MARN) and the Ministry of Economy (MINEC) are preparing to conduct a nation-wide study of the potential benefits and environmental impact of mining before approving any individual environmental permit requests. MARN Executive Director Oscar Diaz told Econoff the ministries were finalizing terms of reference and hope to begin the study during the first trimester of 2008. He suggested the study may yield preliminary results by mid-2008. (Comment: This timetable appears optimistic given the GOES' lack of expertise and funding for the study. The GOES may also prefer to defer politically controversial review of mining policy and approval of mining permits until after the 2009 elections. End Comment.) As of late 2006, there were 36 active concessions for mineral exploration in El Salvador but no active exploitation permits.

MINING FIRMS PRESSURE FOR PERMITS

¶3. U.S. and Canadian mining companies are pressuring the GOES to approve environmental permits and exploitation agreements for gold mining concessions in northern and eastern El Salvador. A Canadian mining company, Pacific Rim Mining Corporation, has grown increasingly frustrated by MARN's failure to approve an environmental permit for its "flagship" El Dorado gold mining project. Pacific Rim has invested \$30 million in exploration and plans to invest an additional \$100 million during the initial phase of the El Dorado project. It estimates that the El Dorado mine will generate 400-600 jobs during construction and 250-270 jobs during operations, all but 5 of which will be done by locals. Pacific Rim has estimated that there is a total potential of 9-15+ million ounces of recoverable gold in El Salvador, with an estimated in situ value of \$5.4-\$9-billion, at a price of \$600/ounce.

¶4. Pacific Rim completed an Environmental Impact Study for the El Dorado project in September 2004. It was approved by MARN in August 2005 and submitted for public comment in October 2005. In a parallel process, the company applied in December 2004 for conversion of its exploration permit to an exploitation license. Pacific Rim's website indicates an anticipate production decision was expected by late 2006, contingent upon approval of its environmental permit and exploitation concession. After two years with little apparent progress on its environmental permit request, Pacific Rim has raised the possibility of filing an investment dispute against the GOES.

¶5. Pacific Rim has consulted with political parties, church leaders and local population adjacent to its mining permit in order to allay environmental concerns and enlist support for its project. Embassy officials have met several times with Pacific Rim officials and have followed up with the MARN, expressing the company's concerns. Pacific Rim argues that the El Dorado project would exploit an underground deposit of low-sulfide deposits with lower environmental risks than open-pit mining of high-sulfide deposits. The company has emphasized its commitment to environmentally responsible mining and has sponsored trips to Chilean gold mines to show legislators how similar mines operate.

¶6. A U.S. mining firm, Commerce Group, has filed a lawsuit against MARN with the Salvadoran Supreme Court after MARN revoked its environmental permit for the San Sebastian gold mine in eastern El Salvador. Commerce Group held the most recent exploitation license, which had been approved in 2002, and re-approved in January 2006. In September 2006, MARN revoked Commerce Group's environmental permit, automatically revoking its exploitation license before it was able to start mining.

NGOS CONTINUE VOCAL OPPOSITION

¶7. Local and international environmental groups have vocally opposed mining projects in El Salvador with some calling for a ban on all mining projects. They argue that the gold mining process carries high risks of contaminating ground water with cyanide and sulfuric acid. Several NGOs, including Share, Caritas, Oxfam and UNES, have helped to organize local demonstrations against mining operations including a December 11 march to call for a moratorium on mining as legislators were holding a mining forum.

¶8. One environmental group, Asociacion de Desarrollo Economico Social, Santa Marta (ADES), commissioned a technical review of Pacific Rim's environmental impact study that criticized technical weaknesses in the study and lack of transparency in the public review process. It faulted the study for failure to include baseline water quality data and estimate water use costs. ADES also cited the GOES failure to include independent data sources in addition to studies contracted by the mining company.

¶9. Environmental groups have continued to criticize a road project funded by the Millennium Challenge Corporation (MCC) which they say will facilitate mining projects. The Share Foundation organized a letter writing campaign to get U.S. Congressional support to stop mining, emphasizing that the industry's practices are counter to the sustainable development goals of the MCC. At post and in Washington, the MCC has met with various NGOs to assure them that there is no connection between the MCC Compact in El Salvador and mining in the country.

¶10. In the legislative assembly, the controversy has generally pitted pro-government legislators open to potential benefits of mining against opposition parties allied with environmental groups. During a mining forum sponsored by the Assembly on December 11, members of the pro-government ARENA, PCN and PDC parties encouraged open discussion of the potential costs and benefits of mining, while some opposition FMLN legislators called for a ban on mining. Two proposals in the legislative assembly would substantially increase royalty payments by mining firms, including one proposal by the pro-government PCN party to increase mining royalties from 2 to 50%. Pacific Rim has enlisted two influential advisors, former Foreign Minister Fidel Chavez Mena and Francisco Escobar Thompson (brother-in-law of Vice President Ana Vilma de Escobar) but has had less success enlisting public support from the opposition.

COMMENT

¶11. Having staked its reputation and company value on its "flagship" El Dorado project, Pacific Rim is understandably impatient to move forward with this project. The GOES has an interest in conducting independent analysis of the mining sector to minimize environmental risks but also needs to maintain clear and consistent rules for investors. In addition to the delays in conducting a mining study, proposals to revise the mining law could

further postpone new exploitation and may affect royalty rates for mining projects. Political controversy appears likely to delay completion of the mining study and issuance of new permits until after the 2009 elections.

GLAZER